BEFORE THE TAX COMMISSION OF THE STATE OF IDAHO

In the Matter of the Protest of	)	
	)	DOCKET NO. 17569
[REDACTED]	)	
	)	DECISION
Petitioner.	)	
	)	

[Redacted] (petitioner) protests the Notice of Deficiency Determination issued by the auditors for the Idaho State Tax Commission (Commission) dated June 5, 2003. The Notice of Deficiency Determination asserted an additional liability for Idaho income tax, penalty, and interest in the total amounts of $42,720 and $51,011 for 1999 and 2000, respectively.

There are two issues to decide in this docket. The first is the extent to which the petitioner had sufficient basis [Redacted] to allow the petitioner to deduct losses from that entity for the years in question. The second issue is whether [Redacted] was a passive activity pursuant to Internal Revenue Code § 469 as to the petitioner.

DETERMINATION OF BASIS

The first issue involves numerous transactions and their effect on the computation of the petitioner's basis in his stock [Redacted] There are numerous transactions which must be considered in making the determination of the basis in question. We will look at each type of contested entry.

One of the factors that makes the computation complex and somewhat confusing is that there are apparently three entities with similar names. The books and records do not appear to adequately separate the entities. From the record there appears to be a [Redacted] the corporation, the basis of which is in question. There is also reference in the records [Redacted] which appear to share a taxpayer identification number (TIN). The TIN used [Redacted] is different from the one

used [Redacted]. Involved in this issue are several deposits to the accounts [Redacted] that the petitioner wishes to be considered to increase his basis [Redacted]. For some deposits that the petitioner wishes to have considered as additions to his basis, the deposit was made, but the source of the funds was not established. For other contested items, only journal entries were supplied. Many such problems were found in the records supplied by the petitioner.

In addition to the problems addressed above, the petitioner has claimed basis for a loan [Redacted]. He contends that the lender looked primarily to him rather than the corporation as the primary obligor on the debt, and therefore he contends that the Commission should allow this as though the debt was from him to the corporation.

The limitation on the allowance of the losses is set out in Internal Revenue Code § 1366 which stated, in part:

> (d) Special rules for losses and deductions.
>
> (1) Cannot exceed shareholder's basis in stock and debt.
>
> The aggregate amount of losses and deductions taken into account by a shareholder under subsection (a) for any taxable year shall not exceed the sum of
>
> (A) the adjusted basis of the shareholder's stock in the S corporation (determined with regard to paragraphs (1) and (2)(A) of section 1367(a) for the taxable year), and
> (B) the shareholder's adjusted basis of any indebtedness of the S corporation to the shareholder (determined without regard to any adjustment under paragraph (2) of section 1367(b) for the taxable year).

The petitioner urges that the Commission follow the findings of Selfe v. United States, 778 F.2d 769, 774 (11th Cir. 1985). In that case, the court found that the loan in truth had been made to the shareholder. In addressing the ruling in Selfe, the 11th Circuit later stated:

> In Selfe, we stated that "arguments similar to [the taxpayer]'s that the taxpayer's guarantee is in reality a loan made to the

> shareholder/taxpayer that is subsequently advanced to the corporation usually meet with little success because the taxpayer is unable to demonstrate that the substance of his transaction is different than its form." 778 F.2d at 774. Appellants have not presented one of the unusual sets of facts that would lead us to conclude that the substance of the SouthTrust loans did not equal their form. We agree with the tax court, therefore, that the Commissioner correctly refused to allow Eli and Peter to include the amounts of the guaranteed loans in their bases in REE and TNE.

Sleiman v. Commissioner, 187 F.3d 1352, 1359 (11th Cir. 1999).

Even when it has been established that there had been a personal guarantee, the vast majority of the cases have held that if there is no economic outlay, there is no addition to the basis. See Sleiman v. Comm'r, 187 F.3d 1352, 1357 (11th Cir. 1999); Bergman v. United States, 174 F.3d 928, 932 (8th Cir. 1999); Uri v. Comm'r, 949 F.2d 371, 373 (10th Cir. 1991); Harris v. U.S., 902 F.2d 439, 443 (5th Cir. 1990); Estate of Leavitt v. Comm'r, 875 F.2d 420, 422 (4th Cir. 1989); Brown v. Comm'r, 706 F.2d 755, 757 (6th Cir. 1983). The Commission finds that the petitioner is not entitled to additional basis due to the debt incurred by CAI until such time as there was such an economic outlay.

The burden of proof for establishing one's right to a deduction is upon the taxpayer:

> Whether and to what extent deductions shall be allowed depends upon legislative grace; and only as there is clear provision therefor can any particular deduction be allowed.
>
> * * *
>
> Obviously, therefore, a taxpayer seeking a deduction must be able to point to an applicable statute and show that he comes within its terms.

New Colonial Ice Co., Inc., v. Helvering, 292 U. S. 435, 440 (1934).

When construing the provisions of the Idaho Income Tax Code, however, we must enforce the law as written. Potlatch Corp. v. Idaho State Tax Comm'n, 128 Idaho 387, 389 (1996); Idaho

State Tax Commission v. Stang, 135 Idaho 800, 802 (2001). The Commission staff has reviewed the information supplied by the petitioner. This review has found that the auditor's determination may have been rather generous based upon the information supplied by the petitioner. Accordingly, the Commission finds that the petitioner has failed to carry his burden of proof in showing that he was entitled to a higher basis [Redacted] than was afforded him by the auditor.

PASSIVE ACTIVITY LOSS

Regarding the second issue, the petitioner's position is that his involvement [Redacted] qualifies as material participation pursuant to section 1.469-5T(a)(4), Income Tax Regulations as a significant participation activity. To establish material participation under section 1.469-5T(a)(4), Income Tax Regulations, the petitioner's activity [Redacted] must constitute a "significant participation" activity under section 1.469-5T(c), Temporary Income Tax Regulations, 53 Fed. Reg. 5726 (Feb. 25, 1988). Furthermore, the petitioner must participate in at least one other significant participation activity, with the total participation in all significant participation activities exceeding 500 hours. A significant participation activity is one in which the taxpayer participates for more than 100 hours, but which fails to constitute material participation under one of the other six tests. Section 1.469-5T(c)(1)(II) and (2), Temporary Income Tax Regulations, *supra*. Thus, in order for an activity to be considered a significant participation activity, the taxpayer (1) must have more than 100 hours of participation; (2) must have less than 500 hours of participation, as participation in excess of 500 hours would satisfy the test contained at section 1.469-5T(a)(1), Temporary Income Tax Regulations, *supra*; and (3) must not be the individual with the most hours of participation in the activity, as a person with the greatest amount of participation in the activity, if in excess of 100 hours, satisfies the test at section 1.469-5T(a)(3), Temporary Income Tax Regulations, *supra*.

The petitioner contends that his hours of activity [Redacted] during 1999 and 2000 were roughly as follows:

	1998	1999	2000
[Redacted]	48	24	12
[Redacted]	4	5	5
[Redacted]	1	1	32
[Redacted]	2	1	1
[Redacted]	4	2	5
[Redacted]	12	4	20
[Redacted]	90	40	36
[Redacted]	16	6	6
[Redacted]	4	4	4
[Redacted]	3	3	3
[Redacted]	8	5	5
[Redacted]	8	6	4
[Redacted]	6	6	6
[Redacted]	50	35	22
[Redacted]	3	2	1
[Redacted]	53		
[Redacted]		65	
[Redacted]			8
TOTALS	312	209	170

The petitioner's testimony with regard to the time spent working [Redacted] is not corroborated by written documentation. The regulations specify that participation in an activity may be established by any reasonable means. While contemporaneous records are not required, reasonable means may include appointment books, calendars, or narrative summaries. Section 1.469-5T(f)(4), Temporary Income Tax Regulations., s*upra*.

Section 1.469-5T(f)(2)(ii)(A), Temporary Income Tax Regulations, provides that work performed by an individual in the individual's capacity as an investor in an activity shall not be treated as participation of the individual in the activity unless the individual is involved in the day-to-day management or operations of the activity. We find that the petitioner was not involved in the day-to-day management or operations [Redacted]. We further find that several of the activities described by the petitioner constitute investor activities, specifically paying bills, reviewing invoices and insurance policies, and the review and computation of taxes. Barniskis v. Commissioner, T. C. Memo 1999-258. Commuting time has also been rejected by the courts in making determinations of material participation. Toups v. Commissioner, T.C. Memo 1993-359; Goshorn v. Commissioner, T. C. Memo 1993-578 footnote 5.

Given the self-serving nature of the petitioner's testimony, coupled with the lack of corroboration in the record, we do not accept his assertion that he worked the requisite amount of hours to qualify his activity as a significant participation activity. Scheiner v. Commissioner, T. C. Memo 1996-554. We are not bound to accept the unverified, undocumented testimony of taxpayers. Hradesky v. Commissioner, 65 T. C. 87, 90 (1975). Although the regulations are somewhat inconclusive concerning the records needed to substantiate material participation, we do not think that they contemplate this type of post-event "ballpark guesstimate" that the petitioner used. Goshorn v. Commissioner, T. C. Memo 1993-578; Speer v. Commissioner, T.C. Memo 1996-323. The petitioner has not met his burden of proving that he met the requirements of section 1.469-5T(a)(4), Temporary Income Tax Regs., *supra*. Chapin v. Commissioner, T. C. Memo 1996-56.

WHEREFORE, the Notice of Deficiency Determination dated June 5, 2003, is hereby APPROVED, AFFIRMED, AND MADE FINAL.

IT IS ORDERED and THIS DOES ORDER that the petitioner pay the following tax, penalty, and interest (calculated to April 15, 2007):

YEAR	TAX	PENALTY	INTEREST	TOTAL
1999	$30,797	$4,620	$14,077	$ 49,494
2000	39,028	5,854	14,717	59,599
				$109,093

DEMAND for immediate payment of the foregoing amount is hereby made and given.

An explanation of the petitioner's right to appeal this decision is enclosed with this decision.

DATED this ____ day of _____, 2007.

IDAHO STATE TAX COMMISSION

_____
COMMISSIONER

CERTIFICATE OF SERVICE

I hereby certify that on this ____ day of _____, 2007, a copy of the within and foregoing DECISION was served by sending the same by United States mail, postage prepaid, in an envelope addressed to:

[REDACTED]
[REDACTED]
[REDACTED]

Receipt No.

_____